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DIRECTORS

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SUPT. LEAF PROCESSING

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COUNSEL

E. A. DARR
MGR. SALES DEPT.

R. J. Reynolds Tobacco Company

WINSTON-SALEM, N. C.

January 12, 1939.

To the Stockholders of
R. J. REYNOLDS TOBACCO COMPANY:

There is submitted herewith the Financial Statement of your Company as of December 31, 1938.

Net earnings for the year 1938 amounted to $23,734,305.75, or $2.37 per share, compared with $27,602,372.38, or $2.76 per share for 1937. Provision has been made for depreciation, taxes and all other charges on the basis which the Company has consistently followed in previous years.

Financial condition of the Company as set forth in the accompanying statement is presented on the same basis as in former reports. The Company's valuable brands, trade-marks and good will are carried, as formerly, in the Financial Statement at the nominal sum of $1.00.

Undivided Profits at December 31, 1938, were $41,584,967.77, as against $40,850,662.02 at the end of the prior year. Net current assets at December 31, 1938, were $136,099,199.57, compared with $114,840,500.36 at the close of the preceding year.

At the end of 1937 the Company had in Current Liabilities, Notes Payable outstanding in the amount of $24,500,000.00, whereas at the end of 1938 the corresponding item was $4,400,000.00. During the summer of 1938, in recognition of the continuance of the desirability of higher inventory investment, for which funds were borrowed in 1937, it was deemed advantageous to convert the principal part of current payables into notes due serially. In August arrangements were made with an insurance company for a loan due over a ten-year period at an interest rate of 2.45% and in October the notes in the amount of $20,000,000.00, as shown under Deferred Liabilities in the Financial Statement, were issued payable $2,000,000.00 per year from 1940 to 1949 inclusive. The advantages of this funding of short-term debt through notes due over a period of years are obvious, particularly in view of the unusually low interest rate offered the Company on this loan.

With a decline in 1938 of more than 20% in total industrial production in the United States, resulting in some shift by consumers to lower-priced products because of the restriction of their purchasing power, the amount of Company sales in 1938, as reported in the Financial Statement, was 6.84% below the amount for 1937. Net earnings for 1938 were 14% below those for 1937. In the year 1938 there were no increases in prices of Company products and the decrease in net earnings at a percentage higher than the percentage of decrease in sales is more than accounted for by four items of expense beyond direct control. These four items of heavier costs were: Increased rate of Federal taxes on income, increase in Social Security tax rates, higher freight charges and greater cost of tobacco used in manufacturing CAMEL Cigarettes, PRINCE ALBERT Smoking Tobacco and other Company brands, which greater cost followed the higher prices paid farmers for leaf tobacco in recent years.

Under the Company's new dividend schedule adopted late in 1937 to facilitate intelligent handling of dividends under the newly enacted Federal Undistributed Profits Tax Law, the dividend declared November 18, 1937, and paid on January 3, 1938, was, in conformity with the handling of January dividends for prior years, deducted from Undivided Profits in the Financial Report for the year 1937, and with only the dividends of February 15th, May 15th, August 15th and November 15th, 1938, charged against Undivided Profits in 1938, it resulted that while stockholders in 1938 received dividends from the Company totaling $2.90 per share, the amount of dividends deducted from Undivided Profits in the Financial Report for 1938 was $2.30 per share. The dividend schedule for 1939 and succeeding years provides for quarterly interim dividend payment dates at February 15th, May 15th, August 15th and November 15th, with a final or year-end dividend payment date at December 26th.

The number of stockholders of the Company has again, in 1938, shown an increase, the total at the end of the year being in excess of 60,000, the largest number in the history of the Company.

Jas. A. Gray,
President.